

## STATE OF ILLINOIS

### ILLINOIS COMMERCE COMMISSION

Northern Illinois Gas Company	)	
d/b/a Nicor Gas Company	)	
	)	Docket No. 08-0363
Proposed general increase in rates, and	)	
revisions to other terms and conditions	)	
of service	)	

### **RESPONSE OF NICOR GAS COMPANY TO STAFF'S MOTION TO STRIKE**

Northern Illinois Gas Company d/b/a Nicor Gas Company ("Nicor Gas" or the "Company"), through its undersigned counsel, hereby responds to the Motion to Strike filed by the Staff of the Illinois Commerce (the "Commission").

#### **I. INTRODUCTION**

Staff asks the Commission to close its eyes. First, Staff objects to the Commission taking administrative notice of the sharp and accelerating fall in the Dow Jones Industrial Average (the "Dow Jones") during 2008. The Dow Jones' plunge and the deepening global economic crisis provided a stark backdrop for this proceeding. In its testimony, Nicor Gas questioned the prudence of Staff's erratic and declining return on equity ("ROE") recommendation in the face of the equity markets' downward spiral. *See* Hawley Sur., Nicor Gas Ex. 35.0, 2:42-3:56, 6:121-24; Fetter Sur., Nicor Gas Ex. 36.0, 3:47-4:71. In its Reply Brief, Nicor Gas juxtaposed the Dow Jones' fall against Staff's declining ROE recommendation. Nicor Gas Reply Br. at 46. The Company's point: Staff modified its calculation methodology and sharply reduced its ROE recommendation with no consideration of "the recent and dramatic events in the U.S. and international financial markets." Fetter Sur., Nicor Gas Ex. 35.0, 6:122-23.

Specifically, Staff objects to the following statement in Nicor Gas' Reply Brief: "To put Ms. Kight-Garlich's revised proposal in a broader context, from August 27, 2008 to October 23, 2008, when Staff filed its Direct and Rebuttal Testimony, the Dow Jones Industrial Average plummeted a sickening 25%." Staff Mot., ¶ 4. Staff offers no authority for its request to strike this sentence. There is none. Well-established law allows the Commission to take administrative notice of current economic conditions and data in its deliberations. 83 Ill. Adm. Code 200.640; *see Peoples Gas Light & Coke Co. v. Slattery*, 373 Ill. 31, 69, 25 N.E.2d 482, 501 (1939); *Island Lake Water Co. v. Ill. Commerce Comm'n*, 65 Ill. App. 3d 853, 857, 382 N.E.2d 835, 839 (2d Dist. 1978). Staff not only fails to cite authority, Staff actually moves to strike Nicor Gas' citation to Section 200.640 of the Commission's Rules of Practice, which expressly authorizes the Commission to take administrative notice of various matters. Staff Mot., ¶ 5. In the alternative, Staff asks to re-open the record, so that it may modify its ROE analysis. *Id.*, ¶ 16. Staff, however, has had every opportunity to present evidence and argument in support of its ROE case. There is no basis for this extraordinary request.

Second, Staff objects to the Company's reference in briefing to the internet address where the Commission might obtain a complete copy the report of the National Action Plan for Energy Efficiency (the "Report"), which Staff witness Peter Lazare quotes in his rate design testimony. Specifically, Staff objects to the statement that:

[A] more complete analysis of the Report[] would have demonstrated that declining rate block structures can promote energy efficiency. Lazare Dir., Staff Ex. 7.0, 36:796-99, *citing* <http://www.epa.gov/cleanrgy/energy-programs/napee/resources/action-plan.html>, Ch. 5, p. 5, fn. 1.

Staff Mot., ¶ 18. Staff, again, provides no authority for its position that the Commission cannot take administrative notice of a technical report, quoted by Staff, which is maintained on the U.S.

Environmental Protection Agency's official website. Indeed, the internet URL address for the entire Report referenced in the Company's Reply Brief was admitted into evidence *by Staff*. See Lazare Dir., Staff Ex. 7.0, 36:785, n. 2. Any argument whether the Commission can take notice of the entire Report reasonably should stop there.

## II. ARGUMENT

### A. Notice of the Dow Jones

The Illinois courts are free to take notice of present economic conditions in their deliberations. *Peoples Gas Light & Coke Co. v. Slattery*, 373 Ill. 31, 69, 25 N.E.2d 482, 501 (1939). The courts also may take notice of economic data by reference to authoritative tabulations of such data. *Island Lake Water Co. v. Ill. Commerce Comm'n*, 65 Ill. App. 3d 853, 857, 382 N.E.2d 835, 839 (2d Dist. 1978) (internal citations omitted). In addition, the courts may take notice of matters of general knowledge and experience; the fact-finder is not required to check its common sense at the courtroom door.<sup>1</sup> By statute, the Commission may take administrative notice of various technical matters within its specialized expertise, as well as "all other matters of which the Circuit Courts of this State may take judicial notice." 83 Ill. Adm. Code 200.640.

Staff cannot seriously question the Commission's authority to take notice of the Dow Jones. In Judge Easterbrook's words, the Dow Jones is "the world's most famous stock market index." *Bd. of Trade of the City Of Chicago v. SEC*, 187 F. 3d 713, 715 (7th Cir. 1999). The courts have recognized the Dow Jones as "the most widely followed indicator of stock prices."

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<sup>1</sup> See, e.g., *Geddes v. Mill Creek Country Club*, 196 Ill. 2d 302, 315-316, 751 N.E.2d 1150, 1158 (2001) ("That golfers do not always hit their golf balls straight is a matter of common knowledge."); *Donehue v. Duvall*, 41 Ill. 2d 377, 379, 243 N.E.2d 222, 224 (Ill. 1968) ("The propensity of small boys to throw things at each other is a matter of common knowledge."); *Fanning v. LeMay*, 38 Ill. 2d 209, 211, 230 N.E.2d 182, 184 (1967) ("It is a matter of common knowledge that shoes are more likely to slip when wet than when dry.").

*Gutierrez v. Deloitte & Touche, L.L.P.*, 147 F. Supp. 2d 584, n.2 (W.D. Texas 2001). The courts also have recognized the Dow Jones as a bellwether economic indicator. “The Dow Jones Industrial Average is followed equally by millions of persons on a regular basis to select investments. Any change, even minuscule, to the Dow Jones Industrial Average, can affect the livelihood of virtually every person worldwide.” *Wendt v. Wendt*, 45 Conn. Supp. 208, 215-16, 706 A.2d 1021, 1025 (S. Ct. Conn. 1996), judgment aff’d, 7575 A.2d 1225 (Conn. App. Sept. 5, 2000), cert. denied (Conn. Dec. 20, 2000).

Nicor Gas used the stomach-turning decline in the equity markets during 2008 to give the Commission a broader context in which to view the prudence of Staff’s ROE recommendation in this proceeding. *See* Hawley Sur., Nicor Gas Ex. 35.0, 2:42-3:56, 6:121-24; Fetter Sur., Nicor Gas Ex. 36.0, 3:47-4:71. On rebuttal, Staff witness Kight-Garlisch devised a new approach to a critical element of the ROE analysis that by her own admission lacked any basis in prior Commission Orders. Tr. at 500:18-501:3. Ms. Kight-Garlisch’s new Capital Asset Pricing Model (“CAPM”) calculation reduced Staff’s overall ROE recommendation from 10.16% to 9.68% between August and October of last year. During the same period, as noted in Nicor Gas Reply Brief, the Dow Jones fell by 25%. Nicor Gas Reply Br. at 46.

The specific facts to be noticed—which are available to anyone at the cost of a few keystrokes—are as follows: On August 27, 2008, the Dow Jones closed at 11,502.51. Staff filed its direct testimony on the same date, recommending a 10.16% ROE. Two months later, on October 23, 2008, Staff filed its rebuttal testimony, recommending a 9.68% ROE based on Ms. Kight-Garlisch’s unprecedented CAPM calculation. On the same date, the Dow Jones closed at 8,691.25, down by 24.44% over the two-month period. The Commission may take

notice that Dow Jones' downward spiral has continued. As of yesterday (February 2, 2009), the Dow Jones closed at 7,936.83, down another 8.68% since Staff filed its rebuttal case.

Staff argues that the Commission must turn a blind eye to the sharply downward direction of the equity markets, because "Nicor Gas failed to link a decline in the Dow Jones Industrials to an increase in utilities' cost of equity generally or Nicor Gas' cost of equity in particular." Staff Mot., ¶ 12. This argument is a red herring. The Commission can and should take notice of current economic conditions and data in its deliberations.<sup>2</sup> Moreover, contrary to Staff's insinuation, Nicor Gas has not and is not asking the Commission to modify Staff's ROE analysis based on information outside the record. Quite the opposite, Nicor Gas is encouraging the Commission to consider Staff's presentation of record—and, in particular, Staff's abrupt change in methodology and sharply reduced ROE recommendation in the middle of this proceeding—in the context of ongoing equity market turmoil.

Staff's argument that it had no opportunity to address this critical point in evidence is simply false. Nicor Gas witness Steven M. Fetter, an expert in utility credit ratings and a former state utility regulator, responded to Ms. Kight-Garlich's sharply revised ROE analysis with the following cautionary testimony:

With the extreme turmoil in the financial markets since [August 27, 2008] regulated utilities appear to have come to a "never before" moment, unless perhaps if one were to look back to the Great Depression. Liquidity, or access to cash when needed, has always been a major issue for regulated utilities, but it has moved

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<sup>2</sup> Section 200.640 provides that the Commission may take administrative notice in a manner "consistent with Section 200.610." 83 Ill. Adm. Code 200.640. Section 200.610 applies the rules of evidence in civil cases in the courts to "contested cases" before the Commission. 83 Ill. Adm. Code 200.610. However, rate cases are excluded from the definition of a "contested case" in the Commission's rules. 83 Ill. Adm. Code 200.40. This exclusion is consistent with the well-recognized axiom that ratemaking is legislative in nature. Attention to economic realities is entirely consistent with the rate making function, whether *sua sponte* or by party motion, and is in no way prohibited by Commission rule or by Illinois law.

to the forefront of utility financial and operational concerns and has driven structural decisions on the part of utility executives.

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[F]ar from supporting a lower authorized ROE in this case, I strongly believe that the current state of affairs within the capital markets dictates a cautionary stance on the part of both Nicor Gas management and the Company's regulators. During the past year, this Commission has authorized ROEs of 10.68% for Ameren's gas operations, 10.30% for Commonwealth Edison's electric distribution activities, and 10.29% for Peoples Gas (reduced to 10.19% owing to a volume balancing adjustment rider)—all ordered before the emergence of the current global credit crisis. For Nicor Gas, which has a history of being the low-cost provider of safe and reliable gas distribution service, sound regulatory policy would dictate developing an ROE that supports a financially sound utility. Unfortunately, and despite current conditions in financial markets, Ms. Kight-Garlich's modified ROE recommendation is going in the wrong direction, which likely will weaken, not strengthen, the Company's financial condition.

Fetter Sur., Nicor Gas Ex. 36.0, 3:50-55, 3:59-4:71. Staff waived cross-examination of Mr. Fetter. Nicor Gas witness Richard L. Hawley also testified in response to Ms. Kight-Garlich's revised ROE analysis. Hawley Sur., Nicor Gas Ex. 35.0, 35.0, 2:42-3:56, 6:121-24. Staff waived Mr. Hawley's cross-examination, too.

Nicor Gas also raised the issue with Ms. Kight-Garlich on her cross-examination. Staff's quotation from the November 19, 2008 hearing takes Ms. Kight-Garlich's testimony out of context. *See* Staff Mot., ¶ 10. The line of questioning sought to show that Ms. Kight-Garlich's decision to take an unprecedented approach to the CAPM component of the ROE analysis on rebuttal was imprudent in light of the equity markets' accelerating decline. A more complete excerpt from Ms. Kight-Garlich's testimony is presented below.

Q. Would you identify another Commission decision that based the CAPM result on raw and adjusted betas?

A. I don't know any other Commission—or I don't know of any Commission decisions that based their decision on raw and adjusted betas.

Q. Not one?

A. No.

Q. Okay. Now, when we started talking, you agreed with me that for a utility to attract common equity capital, it must provide a rate of return on common equity sufficient to meet investor requirements. Do you remember that?

A. Yes.

Q. Okay. And that's because utilities have to compete for capital; right?

A. Yes.

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Q. Would you agree with me that the orders in each of the People's, ComEd, and Ameren cases were entered before or at the beginning of what I think can fairly be described as a very difficult time in the financial markets?

A. No, not entirely. Order -- the last two orders were in September and the -- although the market has continued to decline, that would have still been with the -- difficulty in the financial sector was already occurring at that time.

Q. Would you agree with me that October was a heck of a month in the financial markets?

A. Yeah.

Q. Okay. A heck of a bad month; right?

A. For some companies, but not for every company.

Q. How about for the market as a whole?

A. For the market as a whole, it declined substantially.

Q. Okay. When the Commission -- I think it's probably fair to say when the Commission reaches an approved return on equity, it's not going to make all utilities equal just because they have to compete for investment capital; would you agree with that?

A. What do you mean it won't make all companies equal?

Q. The Commission is not going to set every utility's return on equity at the same rate --

A. No.

Q. -- simply because they have to compete for capital; correct?

A. Correct.

Q. But the relative ability to compete for capital is a consideration; that's fair, isn't it?

A. Yes.

Tr. at 500:18-501:9, 504:17-506:7. The Commission can and should consider this context in its consideration of Staff's ROE analysis.

Moreover, contrary to Staff's assertion, Nicor Gas has not somehow "precluded Staff from reviewing the Company's [ROE] analysis" by referencing the Dow Jones in its Reply Brief. Staff Mot., ¶ 14. This argument does not even make sense. Nicor Gas developed and presented its ROE proposal in this proceeding using the same consistent calculation methodology employed in the Company's 2004 Rate Case, Docket No. 04-0779. Whatever other differences separated Staff and Nicor Gas on the ROE question, abrupt changes in Nicor Gas' methodology during a period of epochal market turmoil was not one of them. In any event, Staff had a complete opportunity to present evidence in response to Nicor Gas' ROE case and to cross-examine the Company's ROE expert, Dr. Jeff D. Makholm. Tr. at 438:13-446:16.

Finally, Nicor Gas objects to Staff's request to re-open the record for purposes of updating Staff's cost of equity analysis. Staff Mot., ¶ 16. Staff already had every opportunity to present evidence and argument on the question.

## **B. Notice of the Report**

Staff moves to strike one sentence from the Company's argument on rate design. In its Initial Brief, Staff claimed that a "substantial body of evidence" warranted rejection of the Company's proposed rate design and a reversal of standing Commission policy. Staff Init. Br. at 85. In response, the Company argued that Staff's "substantial" evidence consisted entirely of three fragmented quotes, found on two pages of one chapter of the Report, contained in its witness Lazare's direct testimony. Nicor Gas Init. Br. at 69.



Specifically, in opposition to the Company's proposed declining block rates, Mr. Lazare testified as follows using selected quotes from the Report:

I share the concern expressed by the previously discussed "National Action Plan for Energy Efficiency" that "rate form like declining block rates... reduce the savings that customer can attain from adopting energy efficiency." The Plan goes on to state with respect to electricity use that as a result of declining block rates, "electricity demand is more likely to increase, which could lead to long-term higher rates and bills where new supply is more costly than energy efficiency."

Lazare Dir., Staff Ex. 7.0, 41:889-95.

Based on Mr. Lazare's testimony, Staff in its Initial Brief questioned the wisdom of Commission policy and prior decisions approving rate designs similar to the Company's proposed declining block rates. Staff Init. Br. at 86. In response, the Company took issue with Staff's claim that "substantial" evidence supports this position by pointing out Staff's extremely limited and one-sided reliance on the Report. Nicor Gas argued that: "[A] a more complete analysis of the Report, would have demonstrated that declining rate block structures can promote efficiency. Lazare Dir., Staff Ex. 7.0, 36:796-99, *citing* <http://www.epa.gov/cleanrgy/energy-programs/napee/resources/action-plan.html>, Ch. 5, p. 5, fn. 1."

Staff objects to the Company's argument because, in Staff's view, "portions of the Report contained in Mr. Lazare's testimony do not support the Company's argument" and "[n]o other portion of the Report is contained within the record." Staff Mot., ¶ 19. Staff also asserts that "[a]ny argument that other parts of the Report, not contained in the Mr. Lazare's testimony, undermine Mr. Lazare's argument in this case, must be disregarded." *Id.*

Staff claims that no portion of the Report relied upon by Mr. Lazare supports the Company's argument that "a more complete analysis of the Report, would have demonstrated

that declining rate block structures can promote efficiency.” Staff Mot., ¶ 19. However, Mr. Lazare’s selective use of the Report does not limit the Commission in its deliberations. The Company’s *argument* simply points out that the Commission, if it were to consider the entire Report, might take a more balanced view of the Report’s effect, if any, on the Company’s declining block rates proposal. Put another way, Staff cannot ask the Commission to consider selected quotations from the Report, admitted into evidence in favor of Staff’s position, without accepting the possibility that the Commission might take notice of the entire document. Staff should have nothing to hide.

### III. CONCLUSION

For all these reasons, Nicor Gas Company respectfully requests that the Commission deny the Motion to Strike filed by the Staff in its entirety.

Dated: February 3, 2009

Respectfully submitted,

NORTHERN ILLINOIS GAS COMPANY  
D/B/A NICOR GAS COMPANY

By: /s/ John E. Rooney  
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**CERTIFICATE OF SERVICE**

I, John E. Rooney, hereby certify that I caused a copy of the Response of Nicor Gas Company to Staff's Motion to Strike to be served upon the service list in Docket No. 08-0363 by email on February 3, 2009.

/s/ John E. Rooney

John E. Rooney